Digital innovation in Asia: What the world can learn

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Companies in the region are transforming their digital operations to great effect and building some of the world's most successful tech giants.

In Asia, a few factors make the impact of digital more pronounced than in other markets, including social penetration, consumers' openness to new technologies and the mobile Internet, and willingness by companies to innovate. In this episode of the *McKinsey Podcast*, McKinsey senior partners Alan Lau and Gregor Theisen talk with Cecilia Ma Zecha about what makes Asia's technological advances different from the rest of the world and the lessons other regions can learn from Asia's innovations.

Podcast transcript

Cecilia Ma Zecha: Welcome to this edition of the *McKinsey Podcast*. I'm Cecilia Ma Zecha, an editor with McKinsey Publishing, based in Singapore. Today we're talking about digital trends in Asia, arguably the hottest region in the world for e-commerce, search, social networking, gaming, and ride sharing, just to name a few.

Asia has its own tech giants, such as China's Tencent, Alibaba, Baidu; Japan's Rakuten and SoftBank, among others. Here to tell us more about Asia's digital landscape and how companies in the region are transforming their digital operations are Alan Lau and Gregor Theisen, senior partners and coleaders of Digital McKinsey in Asia, based in Hong Kong. Alan and Gregor, welcome.

Alan Lau: Thank you.

Cecilia Ma Zecha: Can you start with some level setting on the similarities and the differences between the advance of digitization in Asia and the rest of the world?

Alan Lau: First, there is no one Asia. Economies are vastly different between Japan, Korea versus China, Indonesia, and India. One of the common myths is people think that developing Asia is behind in digital, and I think it's, in fact, the other way around.

The poor legacy in these developing Asian markets, whether it is IT or digital penetration,

or the traditional retail and banking infrastructure, often means that digital is a great opportunity for the country to leapfrog. The most interesting digital market in Asia is actually not the likes of Korea and Japan, but is more China, Indonesia, and India. These are the markets that are really pushing the boundary and innovating the most.

Gregor Theisen: As a Western European, Asia is the most fascinating market I've seen so far, and that's for three major reasons. First of all, it's around innovation. That's not only China—we mentioned all those the companies already—but that's also happening in all the other markets like India or Indonesia.

The second thing is about how they leapfrog technologies. Most of these markets, even though e-commerce or Internet-banking penetration might be low, like in Thailand and Vietnam, social-network penetration is very, very high. It's much higher than in some of the developed markets. In these markets, you find unique business systems and ecosystems, which exploit these opportunities.

The third reason is that the people in these countries, they're open to new technology and mobile Internet. That makes it much easier for businesses to capture the opportunities.

Alan Lau: As Gregor said, these users do not have traditionally great services provided, whether it is in retail, banking, or telecom. When digital tech comes up with new business models, it's often new to these consumers. Therefore, they're more open-minded.

Cecilia Ma Zecha: India has a population of over 1.2 billion, but there's still a lot of potential for growth in broadband usage. There is a call for greater digital infrastructure. So there's still room for digitization to develop in India. Why do you think that that market is leading in innovation?

Alan Lau: If I try to compare India with China, as you said, the digital broadband penetration is still lower, which means that even at this lower level, if we already see this amount of innovation, we definitely can expect more. The other point is, with the attackers in India, they had the opportunity to try something that many Western peers didn't have the need to try before.

For example, look at e-commerce. You have leading companies like Flipkart and Snapdeal. The logistic challenge that they have to deal with is completely different than the UK, Germany, or the US. A lot of times the last-mile delivery is done by people going around on bike, and that really leverages the cheap labor in the country. That's also another reason why markets like India would have the chance to innovate, because they have to innovate. There isn't a lot that they can copy from.

Gregor Theisen: Let me add two points, Alan, regarding what you said about India. My first point is that India has most of the digital talent in the world. It's not only the home of the Internet service providers. These companies focused early on developing digital talent. I would argue we are talking about hundreds of thousands or even millions of talents in that market.

They are driving not only the innovation in India, but they are also the backbone for global innovation. My second point there is, and you touched upon it, yes, of course, there is significant room for improvement regarding the infrastructure side. Broadband Internet access, high-speed mobile phone, or even reliable mobile-phone networks. However, they are moving very fast at least in the key centers and major cities. These markets alone are significant.

A lot of people look at unicorns. Unicorns are defined as privately owned companies with valuations above $1 billion. If you look at the global unicorn landscape, 50–60 percent are based in the US.

The second market then, like Alan said before, is China. The third market is more or less India. You have innovative companies where people believe the valuation justifies their business system and what they are doing. India already has these kind of unicorns there. There are seven, eight, nine of them already, and much more emerging. So I would say, yes, e-commerce penetration is low, around 10 percent. However, Internet banking penetration, at least according to our surveys, is around 18 percent. If you multiply that with the population, it is already a significant market.

Cecilia Ma Zecha: Alan, you've spent a lot of time looking at China. Speaking of a very exceptional entrepreneurial class being an important factor in driving innovation, that certainly is one of the key points of success for the Chinese market. Can you talk more about that?

Alan Lau: The first thing to understand about China is that you don't have the same global names that you see everywhere else. Google, Facebook, Instagram, by and large, are still the leaders in many of the Asian markets. For example the number of Facebook users in Indonesia is larger than the number in the US.

But I think China is the exception. It's a very well-known fact that there is the great firewall, which means that many of these companies' servers are blocked in China. As a result, it has created the environment for the likes of Tencent, Baidu, and Alibaba to rise, starting from about ten years ago. A common myth is people think that these are quick copycat companies that looked to Silicon Valley to import their business model.

Indeed, it may have started that way, but if you look at the past, I would say six, seven years, the market has gone through, and these leaders have done a lot more than just copying. Take Tencent, for example. They have a very popular service called WeChat, which is very similar to a combination of WhatsApp and Facebook. Now they have 700 million users in China. In China, you've also got WhatsApp freely available. But it is WeChat that is, by far, the dominant player.

The Internet leaders in China, like Tencent and Alibaba have really innovated. Yes, they may have drawn the initial inspiration from outside about ten years ago, but certainly in the past couple of years, they've really developed a product and adapted it very much to the local market, to the extent that now a lot of people from outside have been looking to China for inspiration.

Cecilia Ma Zecha: Gregor, the retort is that government protection enables local Chinese firms to thrive, blocks out competition, therefore, Chinese firms don't have to innovate, but instead they copy business models in the West. Is that, like Alan is saying, not giving Chinese tech leaders enough credit?

Gregor Theisen: I fully agree with what Alan said. I'm intrigued by the degree of innovation that is happening in China. These are not only the leaders like Tencent, Baidu, and Alibaba, who have innovated around existing social networks. But it's much more about the businesses around them, for example like in the banking or financial services world.

There are offerings out there in China that are purely based on WeChat. I'm not aware of any other market where we have a WhatsApp bank that is entirely operating in that ecosystem. And that's not only limited to financial services. How people sell and interact via these social networks is also unique. Lastly, what I would love to add is, if they innovate, they innovate at scale. It is rapidly not only a small start-up, it is rapidly an entire business system, with real revenues, real impact, and real clients.

Cecilia Ma Zecha: How has WeChat been able to succeed the way that it has? Essentially turning one app into a full-scale mobile-payment service, whereas many people in the West, for instance, are used to using different apps for different things.

Alan Lau: First, we need to look at WeChat as not just one app. Of course it has a very sticky high-frequency service, which is messaging. But that is just a starting point. It is a super app because it is a portal to many other services that are being offered.

For example, on the main page, you would see the usual messaging interface. It's very similar to WhatsApp. But if you swipe right, then you see many other services that are offered. As Gregor was saying, you can do your banking there. You can shop online. You can get a cab. You can do online payments.

The global discussion and narrative has been around app fatigue. That people have way too many apps on their smartphone. They don't want to be bounced off from one app or one website to another to complete a set of services. In China, it's the opposite. You can get a lot of stuff done on WeChat or Alipay.

Cecilia Ma Zecha: What about the other leaders from China such as Alibaba or Baidu? Anything that they could teach the rest of the world?

Alan Lau: It's also around the theme of ecosystems. Of course, Taobao and Tmall is the traffic driver. Everyone's shopped on it. In fact, the average number of transactions people had on Alibaba is 50 times a year, which means people buy something every week. On top of that, what really facilitates those transactions is Alipay, the payment platform. Alipay is the anchor for Alibaba. They've also developed a whole bunch of services. Very similar to WeChat, you can also shop online. You can get a cab. You can order other local services.

But they are also diversifying from that as well. One of the most fascinating services that

I've seen recently is something called Sesame Credit. In China, most people don't have a credit history. What Alibaba has done with Sesame Credit is to say, "Based on your previous transaction history or borrowing history, I can automatically generate a score for you." If you had a high enough score, that allows you to do things in a more convenient way. So, for example, if you have a score that is above 700, you can book a hotel without making a deposit. If you have a score over 800, you can get a visa to go to Europe without producing income proof. I think if you have a score also around 800, you can get a priority listing on the most popular dating sites in China. They're creating all kinds of new cases, and other new ecosystems.

Gregor Theisen: I always learn when I look into the Chinese market. Every day, every second, there's some innovation happening. I want to step back, and say, yes, of course, these are leading innovators, and they're brilliant ecosystems. They also benefit from the Chinese consumer because they spend more time on the mobile Internet with their smartphone compared to many other markets. In some other markets like Indonesia, they spend even more time. But compared to Western Europe or North America, Chinese consumers spend more time, and they love conveniences like one-stop shopping. We talked about WeChat, Alibaba, all the ecosystems that drive that. But also, the willingness of the consumer. Of course we can learn a lot in the other markets around the ecosystems, what they are offering, and the integration, and the boldness of integrating new business systems.

However, one always has to take into consideration the consumer in the different markets: How will they react? And what will they do? Having said that, there's lots of room for improvement for many other markets and many other players in the other markets. Because even though the consumers don't behave like the Chinese one, they behave in a way that the demand is much higher than the current supply in these markets.

Alan Lau: I really like that point about the open-minded consumer, and I do think it is a key part to the success that we've seen in China. Let's take another service, as an example. Qzone is the equivalent of MySpace, I would say, or of Facebook.

They also have close to 700 million users. There was a lot of debate early on to say, "I just want people to post more photos. How do I do that?" One of the ideas within the company was to say, "I'm just going to auto load the photo and pull it from the photo album into the top of the app, so people can see it." They can just click, and then they can post.

I think many Western counterparts might also come up with the same idea, but it requires someone like a Chinese player to push the boundary. It also required consumers that are open-minded who said, "You're not intruding in my privacy," for that to take off.

Cecilia Ma Zecha: So Korea and Japan are the tech leaders in the minds of many. How are they doing in the advance of digitization in today's world?

Gregor Theisen: Korea and Japan, they have leading tech companies, both of them. Most of the innovation happening there is within the companies, especially on the tech

side; they are leading innovators. However, they don't have this kind of start-up community ecosystem, vibrant community, where lots of innovations are happening.

That is happening much more in the boundaries of existing companies. However, if you look into these markets, they benefit a lot from great infrastructure. They benefit a lot from investments over a certain period of time, because both of these cultures, they are behind new ideas, and they go after these new ideas for multiple years. It's not that you get one year, if it doesn't work, we stop it.

Alan Lau: Korea and Japan are both very interesting markets. Very, very different when it comes to digital because Korea does have a lot of innovation, as Gregor said. Both in a traditional tech site, in hardware, leaders like Samsung and LG. But also in digital.

If you look at some of the global services that they've taken global, like Line, Kakao, these are messaging, but also gaming services that are popular not just in Korea but also outside. In fact, in many parts of Asia their e-commerce penetration is also very high. They just haven't got the same scale as China, as Gregor said. That makes it quite different. I think Japan is a completely different market, and one that I think many people still struggle to understand.

Cecilia Ma Zecha: How is it different?

Alan Lau: It does have major tech companies, admired companies that people have known for decades: Sony, Mitsubishi, Toshiba. But when it comes to digital and IT, and maybe Gregor can add to that, they have been very slow to move.

Legacy IT issues in Japan are probably one of the most challenging as we look across Asian markets. The idea that they need to be disrupting their own businesses and making a lot of changes to the legacy has been slow to catch on.

That doesn't mean that things would not happen. For example, when the iPhone was launched, people also said that it would never take off in Japan because they've got a different system. They've got Docomo. It's a completely different industry environment. But it did take off. When you have a fantastic service, and when you have an innovator that's really pushing a boundary, it will happen. It hasn't happened yet.

Gregor Theisen: And we have another industry, the gaming industry, and especially mobile, online gaming. I would argue that Japan is one of the leading players in that global industry. They are innovating a lot. You see that in certain subsegments of industries, they are able to innovate.

Cecilia Ma Zecha: Increasingly, companies around the world must experiment with digital technology, and, in some cases, reinvent themselves at the core to create new value. Talk about the transformational opportunities and challenges that organizations in Asia face.

Gregor Theisen: First of all, I would separate out emerging Asia from mature Asia

because if you talk about the mature Asian markets and these corporations, at the end, they face exactly the same challenges as American or European companies. They have traditional legacy IT systems. They are in the business for 50 or hundreds of years. They have an existing customer base. They are used to a growth of 2–5 percent per year. These are all very stable environments.

To embark on a digital transformation requires top-down leadership. All functions need to be involved. IT architecture needs to be redesigned. Data architecture needs to be redesigned. But at the end, it is more or less the same as what you do to invest in Europe or in North America with these kind of companies.

If you move to emerging Asia or to conglomerates, which have only a recent history of significant growth, they have one key advantage. The key advantage is no legacy IT. That helps them significantly to leapfrog and embark on a digital transformation journey. The second key advantage most of these companies have is very strong top-down leadership. Some of them are privately owned. They have very visionary leaders. If you embark on an entire transformation of the entire corporation, a visionary leader is extremely helpful, because they inject the entrepreneurial mind-set, exactly what you need to have in order to be successful. So they have an advantage on the legacy IT side, and they have visionary leaders. The third point I would add: there is that you have digital talent available. Even though everybody is looking for digital talent out there, the educational systems, university graduates, they are more and more interested.

They are intrigued. And in my view, they are trained much better to be active and good contributors to a digital transformation than their peers in many other markets. So they have access to a talent pool. They have visionary leaders, and in some markets or some corporations, they don't have legacy IT.

Alan Lau: That's right. There are more similarities than differences when it comes to a digital transformation between Asia and the rest of the world. You still need to recognize that digital is not just having a website or having a social-network account. But it's about digitizing the entire enterprise, as Gregor was saying.

It's digitizing the process, and the customer experience, modernizing your IT, injecting big data analytics and also AI into your core operations. All of that needs to happen. Having visionary leaders, as many Asian companies have, helps tremendously. Many of these are founder-owned companies. They're first-generation entrepreneurs, and they have the skills, and the commitment, to drive through digital transformation.

That's super important. The bottom-up involvement is also critical. Maybe that's where Asian companies are a little bit more different than their Western peers. Because there is still the traditional Asian culture, which is more hierarchical.

Which is, "This is my division. How do I work with them? And do I break the boundary?" One of the terms that we use is you need dragon slayers in the company. The visionary boss needs to empower the digital leader to say, "You need to go work across functions

to do things in a different way and be empowered to do so." This may not always come naturally to Asian cultures. The top-down support would help. But you also need to create that bottom-up culture, and people feel empowered to make changes happen.

Cecilia Ma Zecha: Finally, given everything that we discussed, what would you tell CEOs who are listening to this conversation are the key takeaways when it comes to understanding the digital landscape in this region, and what's distinctive about some of the transformational journeys that are happening within organizations in Asia?

Gregor Theisen: I would say four points. My point number one is if you are a non-Asian CEO or leader, have a close look into Asia and really spend time on the ground. And not only in China. We discussed some other markets like Indonesia and so on, because lots of innovation at scale is happening here.

My second point is, the degree of change and the speed of change is significant. We talked about, we want to be paperless in three years. These are corporations who have 100,000-plus employees. We talked about, I want to reduce my cost base by 90 percent. Again, in three to four years, some significant players. The speed is significant. Learning how they do that, but also thinking about, we think, and I think, they will not only focus on Asia but they will be in Europe and in North America shortly with these kind of offerings.

My third point is how radical some of the players in Asia are. But also for Asian players. If you embark on a digital transformation, go all in. It is not, "Oh, I stop at a certain point in time." You either improve your customer satisfaction and the journeys or you don't. If you just embark on the journey and then stop, because you have traditional channels, sales channels, you have legacy IT, whatever might stop you, then you might be in a worse position.

It is a multiyear journey. It is a top-down journey. But if you embark on it with the entire organization, you will be successful. And the fourth point is, early on, think about the talent, cultural, and organizational implications. What are the new talents I want to integrate? Which ecosystem do I want to be part of? And what are the implications for my organization?

Cecilia Ma Zecha: Alan?

Alan Lau: Gregor covered it very well. I'll just add one point for CEOs, which is, think about your digital board. In a survey that McKinsey did, only about 15 percent of companies said that they actually had a digital-ready board. Only 5 percent of them said they have a technology board. In a rapidly changing environment and paradigm, it is very important to have challenges, to help management stay alert and be updated on what's happening.

That doesn't mean just bring in a token digital native ex-CEO to be on the board, because you wouldn't typically have 11, 15 board members, and just having 1 or 2 is not enough. By all means, bring people in with the relevant experience, but the rest of the board members also need to get upgraded and be aware of the challenges and the opportunity that digital brings. It's important to see Asia as a market where a lot of innovation is happening. People need to come see it. On top of that, don't treat the large Internet companies here, if I take

China as an example, as just competitors. They are your partners.

Cecilia Ma Zecha: Well, thank you, Alan and Gregor, for your insights. And thank you for listening to this conversation. If you'd like to find out more about our research and knowledge, please head over to McKinsey.com. ◻

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